

## MODERN AND FUTURE CHALLENGES FACING AUDITORS IN PUBLIC AND PRIVATE SECTORS IN DEVELOPING AND DEVELOPED COUNTRIES

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**ABSTRACT:** *This paper is to examine the modern and future challenges facing auditors in public and private sectors in developing and developed countries. Auditors today face many challenges and the most important challenges however, is the role of information. Auditors have defined, analyzed and assess the business, though information mirror, the presentation of physical environment in the information, the auditor therefore is a stakeholder in enterprise information integrity failure of business in which deficiencies of financial report and corporate discussion have figured prominent are not new thing. This has been characterized by series of business failure, ethical negligence and accounting scandals both in developed and developing economics. Challenges facing auditors will be necessary to have definition and standards for information integrity and deploy an effective system of automated information controls to monitor monitor, measure and maintain integrity new frontier for auditors.*

**Keywords:** Auditors, Challenges, Information and Integrity

### Preamble

Financial scandals could very easily damage the essence of the auditing profession i.e. public trust' Barker (2002) is the "heartbeat of that profession". Hence, if such trust is betrayed, professional financial, too is destroyed since it would become useless.

Modern and future challenges facing auditing in public and private sector in developing (Malaysia) and developed countries (U.K.) face many challenges. When we say modern we mean present term or recent times and when we say future it means the time that will come after the present. So, when we say modern and future

it means present time and the time that will come after the present challenges facing auditors in public and private sectors in developing and developed countries are the present difficult task that test the ability and skill of the profession in both public and private sectors in developing and developed countries. The purpose of this paper is to promote debate on modern and future challenges in public and private sector in developing and developed countries. The example of developing country we debate on the modern and future challenges facing auditors in Malaysia and in U.K.

## **OBJECTIVES OF THE STUDY**

The following are the objectives

1. To discuss the accelerating changes in the business environment
2. To highlight increasing complexity of system and changes in technologies.
3. To discuss what is wrong with cooperate governance
4. To describe received value of the audit function and hindsight evaluates of auditors performance
5. To discuss the global competition for human capital and audit fees versus audit quality.
6. To make recommendation based on the finding.

## **LITERATURE REVIEW**

Madhavan (2011) says that Auditors to day face many challenges: accelerating changes in the business environment, increase complexity of system and technology and an expanding array of regulations and compliance requirements. The most important challenges however, is the role of information. The physical organization and operation customers, suppliers, people, process and resources are becoming less viable, identifiable and accessible instead, they are represented by the information in Corporate data warehouse. Auditors have defined, analyzed and assess he business, through information Mirror, the representation of physical environment in the information environment the auditor therefore is a stakeholder in Enterprise information integrity.

Perry (2004) also says that one key themes in the challenges is that of independence, including that of professional, such as accountants and directors serving an audit committee.

### **Director and Auditor independence Related issues**

The admirable enhancement of standards for independence, certain basic questions structural ones remain in place. For example the dynamics surrounding the fact that not understanding the clear legal mandate regarding directors” duties common practice has been that the company make the truly important decisions including those about nominee for directorship and about potential auditing firm. Further even where

authority is formally rested in the directors or a committee to chose the accounting firm or in the directors and shareholders new directors, it has often been true that management made the initial choice and promoted that choice to the formal decision makers. Some commentators have concluded that the tendency of directors and possibly other such as attorneys and auditors, to agree with the position and recommendation of many event denies in part from “polanjation” genetics” that is managers, auditing professionals and directors often know one another , personally and professionally, and even if they do not, they will probably share the same values, educational backgrounds and this think similarly. In this regard, one could ask whether, as a practical matter, any of the people typically chosen could even be truly independent.

Millichamp (2000) also mentioned that the problems with audits and auditors are identified as orientation, pressure on the independence or auditors, other stakeholders are interested. In the result of an audit gaps in the audit on propriety future prospects, risk, fraud, internal control and interim and other reports, uninformative auditors reports, competition between auditors lowering standards and integrity, team of litigation, flexible accounting standards, sudden collapses of listed companies; lack of hospital regulation.

The recent accounting scandals in developing countries not any adversely eroded trust of the shareholder and

stakeholders in the affected companies but also affected the integrity of the capital market, the regulators and auditing profession. So as far as the audit profession is concerned, if that indeed the case interested parties may need to be an highest alert for as mentioned by Railborn and Schorg (2004), the presence of growing distrust in the auditing profession may well be a cancer that is metastasis”.

### **Accelerating Changes**

“We are entering an age of acceleration. The models underlying society at every level, which are largely based on a linear model of change, are going to have to be redefined. Because of the explosive power of exponential growth, the 21<sup>st</sup> century will be equivalent to 20,000 years of progress at today’s rate of pace”, said Ray Kurzweil, inventor, entrepreneur, author and futurist.

This rapid acceleration of change is manifested by the revolutionary trends in the business environment.

- Globalization of manufacturing
- Business process outstanding
- Transnational mergers and acquisitions
- Privatization of many public sector activities
- Deregulation
- Rapid growth in access and use of the internet
- Emergence of internet based business such as internet banking, e-commerce, etc.
- Doubling of the total volume of information every 24 months.

An important consequence of these changes is the necessity or relying on information from third-parties to operate, manage and monitor the business. This creates new challenges for the internal auditor.

Even more important is the fact that the pace of these changes is only going to accelerate even further in the future.

### **Increasing Complexity**

Challenges in technologies, new business models, increased business activity, mergers, consolidations, privatization, deregulation, etc have resulted in significantly increasing the complexity of the business environments and the associated information systems and technologies supporting them. This complexity manifests self in many forms affecting everything from the day-to-day operations of the business to senior management’s strategic plans. Economies of scale, scope and skills appear to be wiped out by ‘economies of complexity’

Complexity is a hidden cost of doing business. Complexity has created a many headed monster for management. Excessive complexity typically grows over many years and fossilizes into structures, cultures, systems, and complexity poses significant challenges to internal audit’s ability to provide assurances on the achievability of organizational objectives. Modern enterprises operate in a connected economy. They constantly generate, use, store, and exchange information and materials with customers, partners, and suppliers. Enterprises are also required to exchange key performance information with the regulatory agencies and the shareholders., the connected enterprises can only be successful I if it provides and receives the accurate information it needs in order to do business effectively. Trustworthy information reduces uncertainty in the decision-making process, enhance confidence, and improves operational effectiveness.

The internal audit community needs a framework and a set of tools to understand and examine the information flows within a complex environment in order to provide assurance over compliance and business objectives. The existing framework and

tools are not adequate as evidenced by the number of business failure.

### **The future of auditing**

1. The legal framework of auditing is subject to periodic change as new companies Acts are promulgated. The theory and practice of auditing is being steadily developed by the Professional bodies and now the Auditing Practices Board. New developments occur because of new situations and ever rising expectations and the need for higher standards.
2. Most developments in auditing have been evolutionary but currently more rapid change, which might be called revolutionary, is about to happen. This has primarily come about because of public attention on the whole way in which companies are run and governed. There have been many listed companies which have collapsed suddenly and many of these have been run in a dictatorial manner by one strong character.
3. As a response to these problems in the governance of companies, the Cadbury Committee was set up and reported in late 1992 in 'The report of the Committee on the Financial Aspects of Corporate Governance'. This report recommended many changes in the board rooms, reporting practices and auditing including a Code of Best Practice. The ramifications of the Cadbury Code on Corporate Governance are still being worked out and they have a substantial impact on the future of auditing in the short term.
4. The auditing Practices Board issued a paper on 'The Future Development of Auditing' in November 1992. The purpose of this paper is to promote debate on the future of auditing in

the UK and Ireland. This paper is also reviewed in this chapter. The auditing practices Committee produced a further document 'The Audit Agenda' in December 1994 and we will review it also.

### **What is wrong with corporate governance?**

Public attention has been focused on Corporate Governance (the action, manner or system of governing) and especially the financial aspects for several reasons including:

- a. The collapse of several large companies without warning.
- b. Concern about standards of financial reporting (the Financial Reporting Review Panel have reported several 'profits' which had to be modified).
- c. Lack of accountability by companies run by dominant characters
- d. Raids on company pension schemes by companies in financial difficulties
- e. Apparently excessive directors pay, the rates of which seem to be fixed by the recipients themselves. Excessive severance pay for directors. The Greenbury committee reported on this in 1995.
- f. Some notable frauds and incidents of insider trading
- g. A feeling that auditors cannot stand up to demand Boards.
- h. A feeling that auditors are too close to their clients as a result of carrying out such non-audit work.
- i. Looseness of accounting standards
- j. The practice of opinion shopping where companies seek auditors who will agree with them.
- k. The expectations gap where the investing public does not understand the rather limited role of the auditor and imagines he/she is doing much more especially in the area of fraud.

5. Already there had been improvements including the Companies Acts of 1985 and 1989 with the whole panoply of regulation of auditors and the setting up of the Financial Reporting Council with the Accounting Standards Board, the Urgent Issues Task Force and the Financial Reporting Review Panel. There is also the Auditing Practices Board which is improving auditing practice.

- 6.

#### **LOW PERCEIVED VALUE OF THE AUDIT FUNCTION**

One of the challenges facing audit practitioner in developing countries is the low perceived value of the audit function. In short, for many of the small audit clients of the auditors interviewed, company auditing is viewed as a waste of money and resources.

From the theoretical perspective, the need of an audit function can be explained by the agency theory, which denotes that due to a separation of ownership and control, the principal (owner) will monitor the activities of management through an audit function. However, in Malaysia, an audit is mandatory for all companies despite their size and ownership structure (i.e. private or public companies). Notwithstanding the compulsory audit requirement, many auditors have pointed out that the actual contribution of auditing towards its intended purposes is somehow limited. This is because a vast majority of the companies in Malaysia are private companies as opposed to public companies. Furthermore, a majority of these private companies are owner-managed. Hence, an audit appears to be meaningless to most of the private companies because the directors and the shareholders are basically the same people.

For this very reason, it explains why most audit clients have found an audit function as a non-value adding activity and perceive it to be a costly process. As pointed out by a number of auditors, the most

prominent value of auditing for the private companies is merely adding credibility to the financial statements for the purpose of tax submission to the Inland Revenue Board (IRB) and that of loan applications to the financial institutions.

On the other hand, many auditors agree that an audit function has a more significant role for public companies since it serves the purpose of reporting to their existing shareholders and attracting future investment. In the final analysis, some auditors are of the opinion that the practical usefulness of auditing may only be applicable to a limited group of users such as bankers, institutional investors and regulatory bodies. They have also argued that a large section of the Malaysian public do not actually rely on the audited financial statements for decision-making. As a result, over the years, it can be witnessed that the practice of auditing has gained little perceived recognition from a large section of the Malaysian public.

#### **Hindsight evaluation of auditors' performance**

Another problem underlying the audit practice in Malaysia is the inability of the public to make a fair evaluation of auditors' performance. On the whole, audit practitioners claim that the present deluge of accusations against auditors is largely associated with the recent financial scandals at Transmile and Megan Media. They point out that this is to be expected: it is the Malaysian habit to accuse the auditors of failing to perform their work diligently whenever a corporate financial scandal hits the news. In their view, this is because the public do not have the necessary knowledge and ability to evaluate the quality of an audit



leading to a situation of failing to differentiate between the quality of one audit versus another. These auditors argue that the public judgment of audit quality will only come out as a result of subsequent events which more often than not is demonstrated through negative reporting by the media that an audit has not quite been performed at an acceptable level! The hindsight evaluation of auditors is deemed to be unfair as the perceived quality of the auditors has been judged using the benefit of knowledge after the event has taken place to argue that auditors are not performing adequately

The hindsight manner of evaluation is likely to bring about a high level of criticism against the auditors given the significant amount of negative publicity they receive. In actual fact, the blame should not be placed on the auditors' shoulder alone whenever a corporation is in trouble. This is simply because there are many other reasons which may lead to the emergence of such a corporate quagmire including mismanagement, bad strategic decisions, industry downturns, competition, poor oversight by the board of directors and last but certainly not least fraud by senior management.

Since old habits die hard, notwithstanding the presence of these and other debilitating factors, the Malaysian public may continue to apply the hindsight manner of evaluation of auditors' performance and accordingly blame the auditors after just about every disclosure of corporate debacle. In doing so, as argued by an auditor, the public is in need to be reminded with one important fact: the number of alleged audit failures as compared to the number of audit cases conducted over the years in the country is really quite small. Hence, the terrible accusation thrown against the audit profession in the country as a result of a few bad apples does not seem to be reasonable at all.

### **Global competition for human capital**

Human capital is the most important and essential asset and sourcing for real talent is posing to be a great challenge for the auditing industry. Unlike other industries where technological advancement may help to reduce human capital needed, the auditing industry is similar to other service-based industries, which tend to be labour intensive. An auditor has pointed this out by saying that the forming of an independent opinion whether the financial statements give a true and fair view is a process that requires much subjective judgment. Such a task needs to be performed by professional audit personnel. Therefore, "people" are always important for the success of an audit firm.

In recent years, globalization has gained widespread impact on the financial sector in Malaysia. As far as the audit profession in Malaysia is concerned, it has now had to face global competition for human capital. One of the auditors pointed out that local audit firms are now facing a tough time in recruiting qualified auditing personnel as they are paid much better in countries like Singapore, China and the Middle East. According to him a qualified audit personnel is paid double in Singapore and four to five times in China and the Middle East. This in his view can only mean more headache for audit proprietors and partners who for many years now have already had to confront the view held by fresh accounting graduates that auditing is a less attractive profession due to its long working hours and less lucrative remuneration.

Another auditor claims that the shortage of auditing staff has caused an unhealthy competition among audit firms in Malaysia particularly for young graduates. He explained, audit firms are supposed to be training providers for novices to gain the necessary knowledge and experience; however, the switching of jobs rapidly by the so-called new accountants across a

number of audit firms will certainly jeopardise their learning process.

### **Modern and future challenges facing Auditors in Nigeria**

Failures of business in which deficiencies of financial report and corporate disclosure have figured prominently are not new phenomena. This period has been characterized by series of business failure, ethical negligence and accounting scandals both in developed and developing economies.

Publicized cases of recent past, such as Cadbury and NAMPAC in Nigeria have drawn increasing attention to the auditing profession. This has had a negative and cumulative impact on the way informed opinion views financial reporting and auditing profession. There has been great apprehension regarding the fairness of the operation of market system where shareholders, employees in general and pensioners have lost large sums, while those running companies and seen as responsible for those losses, have enriched themselves as the business collapsed (Adeyemi 2011).

However, Nigeria Accountants and Auditors are experiencing challenges which question the trustworthiness and integrity of profession. According to Hale et al (2005), has been eroding the confidence that the public repose on the auditing profession. Regulatory Initiatives have been put in place in developed economies to deal with the poignant erosion of ethical standards in corporate governance, financial reporting and auditing. For example, in United States of America, the Sarbanes Oxley Act was passed into law in 2002, the International Federation of Accountants (IFAC) has also supported the formulation of auditing guidelines to enhance the reliability of corporate financial statements. The International Accounting Standards Board has consistently stressed the need for global adopting of the International Financial

Reporting Standards. However, the developing economies, including Nigeria, there has been little or no efforts at positively addressing challenges posed by non-adherence to corporate governance principles and ethical guidelines. For example Nigeria is yet to review its Companies and Allied Matters Act 1990 (as amended) which has become more or less anachronistic in view of dynamic corporate events. Bakre (2007) reported that investors in Nigeria have lost several billions of dollars through the collusion of accountants and external auditor with the companies management and directors to falsify and deliberately overstate companies accounts. Adelaja (2009) in evaluating the perception of auditor independence in Nigeria concludes that all efforts must afloat on matters of ethics and independence. It is however, in doubt if Nigerian related research efforts are adequate to fully address the challenges of enforcing ethical guidelines in financial reporting and auditing.

### **Ethical question of integrity**

In many cases Auditors see themselves as employees or agent of their client on the one hand, such attitude is quite understandable and predictable. On the other hand, it seems to be undermining the notions of independence and objectivity that have so long marked the profession of advocacy. Today, major auditing firms will offer cafeteria of financial services, will offer virtually anything a client wants without necessarily thinking of how it affects the culture of their professional calling.

Moreso, the issue of non-qualification of Financial Reports it is a common knowledge here in Nigeria that, a large percentage of Auditors' report are not qualified. It does not mean that all these statement are not qualifiable but the matter lie with the auditor who did the audit job. As a result of unqualified financial statements, the general

public assume that all is well and continue to make investment. By this the auditor had abused the ethics of independence and objectivity. It is as a result of this that the issue of the distress in the banking industry from 1996 to date came to focus. A look at this will reveal that if there were not ethical abuses most of the distressed banks would have been saved. Resulting from the above, the professional once ran into crisis which almost got her integrity eroded, and this was when auditors and the legal profession had a face-off in the issue of lawyers' attestation. Finally, lawyer's attestation to Auditor's report. For the first time in history, a controversy was created between the auditors and the law profession in Nigeria as a result of section 359(2) of Companies and Allied Matters Decree (1990) which authorized lawyers to countersign auditor's report. The argument put forward in support of that section was that auditors are skilled professionals who, by their technical knowhow collude with companies to produce different sets of Accounts of a particular period different for different purposes. The provision was perceived by Accountants as the efforts of those in legal profession to create avenue to fend for their hungry members, since they would, of course, charge fees for countersigning the auditor's report. They could thus be reaping from where they have not sown. The Institute of Chartered Accountants of Nigeria and every other recognized accounting professional bodies other institutes and personality firmly opposed the provision which the repeal of the Section 359(2) of the Decree (Oni et al 2011).

### Summary

There is general disquiet about the governance of companies and of other entities with public profile.

The integrity of the information and information and information environment in

most organization today is often unclear, ill-defined or at best suspect.

Nevertheless, it should be noted that stronger regulation may not be the only solution in providing better audit practice in both developed and developing countries

### Conclusion

All in all, given the private sector in developing and developed countries, the reforms include amending related legislation and enforcing a higher degree of regulation. In particular, with implantation of the practice review and financial statement review by MIA, the conduct profession may now be considered to be highly regulate.

### Recommendation

I therefore recommend that all the challenges facing auditors' will be necessary to have definition and standards for information integrity and deploy an effective system of automated information controls to monitor, measure and maintain information integrity new frontier for auditors.

Moreso, new definition enlarging the scope of audits to proper conduct and future risks, enlarging reporting responsibilities to all published statements, financial controls, propriety, efficiency, fraud illegality; assumptions and judgment underlying the accounts more informative reporting by auditors, more duting to other stakeholders, improving the independence of auditors; involving shareholder with the auditors.

Finally, educating society on the nature and purpose of an audit may actually help the public recognize the value of

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